

Message Text

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C O N F I D E N T I A L JIDDA 1173

E.O. 11652: GDS

TAGS: EFIN, EIND, SA

SUBJECT: SAUDIS TIGHTEN CONTRACT EVALUATION

1. COMMERCIAL BANKING OFFICIALS TOLD EMBOFFS FEB 9 THAT CROWN PRINCE FAHD ISSUED A MEMORANDUM WITHIN THE LAST TEN DAYS TO ALL MINISTERS DECRYING THE EXCESSIVE PRICE OF BIDS BEING RECEIVED ON GOVERNMENT TENDERS. THE MEMORANDUM REPORTEDLY INSTRUCTED ALL MINISTERS TO GIVE A HARD LOOK AT ALL BIDS RECEIVED SINCE CONTRACTORS ON FIXED COST BIDS WERE SIGNIFICANTLY OVER-COMPENSATING FOR ANTICIPATED INFLATION. SPECIFICALLY, MINISTRIES WERE INSTRUCTED TO REJECT ANY AND ALL BIDS WHICH APPEARED TO BE UNREASONABLE. THE REJECTION OF A SERIES OF TENDERS FOR ELECTRICAL PROJECTS BY MINISTER OF INDUSTRY AND ELECTRICITY GHAZI AL GOSAIBI WAS REPORTEDLY A DIRECT RESULT OF THE FAHD DIRECTIVE. THE REJECTIONS TOOK PLACE ON FEBRUARY 7.

2. PROJECTS REJECTED BY AL GOSAIBI WERE FOR POWER GENERATION IN AL-KHARJ, AL-WAHNA, JIZAN AND ASSIR. PRESS REPORTS QUOTED THE MINISTER AS STATING THAT THE EIGHT BIDS RECEIVED ON THESE PROJECTS WERE FAR HIGHER THAN THE ELECTRICITY AUTHORITY'S OWN ESTIMATES. WHILE GOSAIBI STATED THAT HIS DECISION WAS SUPPORTED BY KING KHALED AND CROWN PRINCE FAHD, NO REFERENCE WAS MADE TO A FORMAL DIRECTIVE FROM FAHD.

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3. ACCORDING TO THE ARAB NEWS ON 8 FEBRUARY, MINISTER GOSAIBI WILL SEARCH OUT NEW BIDDERS FOR THE ELECTRICAL PROJECTS AND WILL DEPRIVE COMPANIES WHO OFFER UNJUSTIFIED BIDS IN THE FUTURE FROM EVEN BIDDING ON CONTRACTS. (THIS LAST PROVISION APPEARS TO BE AT GOSAIBI'S -- NOT FAHD'S INITIATIVE). SUBSEQUENT REPORTS IN THE ARAB NEWS

ON 10 FEBRUARY INDICATE THAT THE EIGHT UNSUCCESSFUL BIDDERS INCLUDED AMERICAN, EUROPEAN AND JAPANESE FIRMS. THE FOLLOW-UP REPORT ALSO DISCLOSED THAT AL-GOSAIBI WILL TRAVEL LATER THIS MONTH AND IN MARCH TO INDIA, PAKISTAN, SOUTH KOREA AND TAIWAN TO SEEK NEW BIDS FOR THE PROJECTS.

4. COMMENT: THESE DEVELOPMENTS PROBABLY REFLECT A GROWING SAG AWARENESS THAT THEIR RESISTANCE TO COST-PLUS CONTRACTING HAS LED TO EXCESSIVE PADDING BY BIDDERS TO PROTECT THEMSELVES FROM THE UNCERTAINTY AND RISK OF POTENTIAL PRICE COST ESCALATION. THE SAG FEELS THAT IT IS DOING EVERYTHING POSSIBLE TO HOLD BACK INFLATION THROUGH THE COMBINED USE OF SPENDING CONSTRAINTS AND SUBSIDIES. ON THE BASIS OF THIRD QUARTER 1976 DATA, SAG FEELS THAT IT IS IN FACT COMING TO GRIPS WITH THE PROBLEM. WITH THIS IN MIND, THE SAG'S TIMING OF A NEW DRIVE TO HOLD DOWN CONTRACT PRICES IS UNDERSTANDABLE. FUTURE COST TRENDS ARE STILL VERY UNCERTAIN IN SAUDI ARABIA, HOWEVER, AND MANY FIRMS MAY FIND THAT BIDS WILL ONLY BE ACCEPTABLE ON A COST PLUS BASIS. WHILE THE SAUDIS RECOGNIZE THIS, THEY STILL LACK THE MANPOWER AND ADMINISTRATIVE SKILL NEEDED TO SUCCESSFULLY MONITOR THE MYRIAD OF CONTRACTS BEING UNDERTAKEN IF ALL OR EVEN THE BULK OF THEM WERE TO BE ON A COST-PLUS BASIS.
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